Attachment #9

COUNTY OF SAN LUIS OBISPO

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To: County of San Luis Obispo Board of Supervisors

From: James P. Erb, Auditor-Controller-Treasurer-Tax Collector

Date: May 17, 2016

Subject: Pension Obligation Bond (POB) Lump Sum Funding Proposal

Recommendation:
It is recommended that the Board:

1) Approve the financing plan to fully fund the 2009 Series A POB final payment of $42,565,000 by September 1, 2019;

2) Authorize the Auditor-Controller-Treasurer-Tax Collector to transfer the amounts identified in the transfer schedule included in the “Financial Considerations” section of this report to a designation established in the POB Debt Service Fund in preparation for the September 1, 2019 lump sum payment; and

3) Authorize the Auditor-Controller-Treasurer-Tax Collector to use the funds in the POB designation to pay off the 2009 Series A Pension Obligation Bonds on September 1, 2019 or sooner as required by the Bond Trustee’s funding instructions.

4) Approve a budget adjustment in the amount of $9,688,657 to transfer funds from the General Fund POB designation to the POB debt service fund where it will be used to increase the amount set aside to pay off the 2009 Series A Pension Obligation Bonds.

Background:

In 2003, the County issued $137,194,398 of Pension Obligation Bonds (POBs) in three unique series to reduce the balance owed to San Luis Obispo County Pension Trust (SLOCPT) for unfunded pension liability. The POBs were issued at interest rates lower than the SLOCPT assumed earnings rate of 7.75% (currently 7.25%). The bonds were issued at rates between 1.68% and 5.73%. A brief description of each of the series follows:

2003 Series A (Standard Bonds); includes an annual principal and interest payment and is scheduled for a final payment in September 2017. The annual debt service payment is budgeted each year. Over the 15 year life of the 2003 Series A, the County will have paid

$44,305,000 in principal and $13,936,116 in interest. Interest rates for this series range between 1.68% and 4.54%.

2003 Series B (Auction Rate Securities); were issued at fixed interest rates of 2.36% fixed until 2006. In 2006 the bonds were reset and each year thereafter go through an auction process. In the event no one purchased the bonds the rate jumped to roughly 17% or three times the Libor Index. In 2008, the County's auction rate securities failed to be purchased by an investor. The County was fortunately able to refinance the auction rate securities with the 2009 Series A (interest only) POB rather than paying the higher default rate. The new series (2009 Series A) is discussed below.

2003 Series C (Capital Appreciation Bonds); are a deferred debt instrument. Principal and interest payments begin on September 1, 2018 with the final payment on September 1, 2030. These bonds cannot be retired early. The annual debt service payment will be a part of each year's budget appropriation.

2009 Series A (Interest Only Bonds); replaced the 2003 Series B auction rate securities. The payments are interest only at a fixed rate of 7.45% due annually for 10 years. The final payment is due on September 1, 2019 and will include the deferred principal amount of $42,565,000.

It is critical that the County begin planning for the retirement of the 2009 Series A Bonds as soon as possible. We have identified three options to consider. The options are: 1) pay the balance in full; 2) pay a portion of the balance and refinance the remaining principal; or 3) refinance the entire principal amount of $42,565,000. My recommendation is to pay the balance in full using funds set aside in a designation.

Other Agency Involvement:

The budget considerations have been reviewed with the Administrative Office. The Auditor-Controller-Treasurer-Tax Collector's Office will notify the other agencies participating in the annual POB payments that each is responsible for a portion of the $42,565,000 obligation due on September 1, 2019. Based on the Final Actuarial Valuation Report for the year beginning January 1, 2015, the Schedule of Employer Allocations breaks out the percentages by agency as follows: San Luis Obispo County (92.6481%), San Luis Obispo Superior Courts (5.6757%), Air Pollution Control District (1.1591%), San Luis Obispo Pension Trust (.3318%), and Local Agency Formation Commission (.1853%). The participants could have the option of paying a flat dollar amount associated with their share by September 1, 2019 or repaying the POB fund over 15 years to coincide with the payments of the 2003 Series C (CAB). Their share of the lump sum payment will be based on the most current percentages available.

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Financial Considerations:

The County has currently set aside $19,449,428 in designations for the purpose of paying the 2009 Series A POB lump sum payment. It is recommended that remaining amount required be funded from the Tax Loss Reserve Fund (TLRF), the Teeter Fund, and the POB debt service fund.

Both the Teeter Fund and TLRF were established when the County implemented the Teeter Plan in July 1993. The Teeter Plan allows the County to finance property tax receipts for local agencies by borrowing money to advance cash to each taxing jurisdiction in an amount equal to the current year's delinquent property taxes. Local agencies benefit as their budgets are known at the beginning of the year and actual property tax revenue will not fluctuate based on delinquent payments. In exchange, the County receives the penalties and interest on delinquent taxes when collected. Those delinquent penalties and interest are deposited in the TLRF. Currently, every taxing jurisdiction in the County participates in the Teeter Plan.

The Teeter Fund is used for the annual buyout of delinquent property taxes to the local taxing jurisdictions. If needed, the County can issue a one year note from the Treasury Pool to finance the Teeter buyout. The Teeter Fund also captures delinquent general fund property taxes. The Teeter Fund has averaged a positive return over the last 8 years of $2.5 million. However, as the economy improves, the amount collected in both delinquent taxes and penalties and interest will continue to decline. The financing plan provided below factors in expected declining growth of the fund and existing balances.

The TLRF is where penalties and interest collected on delinquent taxes are accumulated. The TLRF's annual receipts averaged $2,465,034 over the last 8 years. Approximately $1.9 million of the annual receipts is allocated to the current budget. The financing plan provided below factors in an expected decline in growth of the fund and existing balances. Also factored in is the requirement to maintain a reserve balance equal to 25% of the delinquent secured roll at year end.

Transfer Schedule	**Action**	**From Fund**	**Account Name**		**Amount**
Beginning Balance		POB – Debt Service Fund (DSF)	Designation for POB Debt Service	$	9,760,771
July 1, 2016	Move to DSF POB Designation	General Fund	Designation for POB Obligation		9,688,657
July 1, 2016	Move to DSF POB Designation	Tax Loss Reserve Fund	Fund Balance Available		2,054,317
July 1, 2016	Move to DSF POB Designation	Teeter Fund	Fund Balance Available		2,410,042
July 1, 2016	Move to DSF POB Designation	Teeter Fund	Interest Earned		5,258,134
July 1, 2017	Move to DSF POB Designation	Tax Loss Reserve Fund	Fund Balance Available		2,054,317

July 1, 2017	Move to DSF POB Designation	Teeter Fund	Fund Balance Available		2,410,042
July 1, 2018	Move to DSF POB Designation	Tax Loss Reserve Fund	Fund Balance Available		2,054,317
July 1, 2018	Move to DSF POB Designation	Teeter Fund	Fund Balance Available		2,410,043
July 1, 2019	Move to DSF POB Designation	Tax Loss Reserve Fund	Fund Balance Available		2,054,317
July 1, 2019	Move to DSF POB Designation	Teeter Fund	Fund Balance Available		2,410,043
Total Available				$	42,565,000
September 1, 2019	Payment to Bond Trustee	POB Debt Service Fund	Designation for POB Debt Service	$	42,565,000

Results:

Paying the entire principal balance will avoid over $18 million dollars of interest if the County were able to refinance straight line at 5% for 15 years. At 7% the interest paid would be over $26 million. In addition, reducing the County's debt helps the County maintain strong credit ratings.